

Budget 2004

Budget Assessment

Introduction

This was a confident and optimistic Budget. The most significant announcements were on public spending – the welcome increase in education spending and the less welcome cuts in some civil service jobs. Suggestions that the Chancellor needed to put up tax to meet his public spending plans were firmly rejected – indeed, the Budget speech went out of its way to emphasise that tax rates were on hold. But there also some significant omissions - there was very little in the Budget for manufacturing or for women and pensions.

The economy

The economic forecasts are virtually unchanged from the Pre Budget Report – hardly surprising given they were only published three months ago. The overall economy is forecast to grow strongly by over 3 per cent in both 2004 and 2005. Our economic judgement is also unchanged – we fully expect the growth forecasts to be met.

Manufacturing is also forecast to recover, but the Treasury is taking a more cautious line than some of the more bullish recent forecasts. We think the Treasury is right to be cautious. Latest figures for manufacturing output growth, investment levels and export performance give cause for concern about the robustness of the current recovery. However, this makes it all the more disappointing that there was so little specifically aimed at the manufacturing sector in this Budget.

Public finances and public spending

The projections for the public finances are much the same as in the Pre Budget Report. The Chancellor borrows very slightly more in the short term to reflect slightly weaker revenues, but in economic terms the increase is not significant. Borrowing is projected to fall rapidly as a share of GDP dropping from 3.4 per cent in 2003-2004 to below 2 per cent by 2007-2008.

Even though the Government is borrowing large sums of money for investment in the public infrastructure, the underlying state of the public finances remains strong. Public debt as share of GDP is projected to remain below 36 per cent, well below

the Chancellor's own fiscal rule of 40 per cent and far below public debt levels across Europe or in the United States or Japan.

The main constraint on the Chancellor is the need to build up surpluses on current spending over the economic cycle. The current projections allow very little room for manoeuvre, with an average surplus of just 0.1 per cent of GDP projected from 2005-2006 onwards. Much depends on the medium term outlook for the economy and the strength of the recovery in tax revenues. But our guess is that the Chancellor will not have much for additional spending in Budget 2005 once the Spending Review is concluded in summer 2004.

The Fourth Spending Review

The Spending Review announcements were by far the most important in this Budget. The key announcements were:

- Over the period covered by the Fourth Review, the overall increase in current spending to be 2.5 per cent, with capital spending increasing much faster so that the share of public investment increases from 2 to 2.25 per cent of GDP;
- The overall increase in total public spending and in Departmental spending will be lower than under the Third Review;
- Within these constraints, the Government has assumed efficiency savings of £20 billion per annum by 2007-2008 so that *“the Governments objective is to match the pace of growth in front line services achieved in the last Spending Review”*;
- The Spending Review allocation to education has been announced early and provides for growth of 4.4 per cent per annum in real terms. This is not quite as fast as the Third Review settlement, but is far in excess of the pre-1997 growth rate of 1.5 per cent per annum;
- There will be real terms spending increases in transport (not that any cuts were expected) and also defence and homeland security will also see real terms increases.

So the scope of the Spending Review will be far narrower than in previous years, now the big budgets of health and education have been pencilled in. The Government is clearly pinning its hopes on the Efficiency Review to reduce the funding constraint on other Departmental Budgets. We comment in more detail on the implications of the Review below.

Efficiency Review

We support the Government's drive to improve public service quality and efficiency by, for example, investing in IT and training and streamlining public procurement and freeing-up the time of front line staff by removing excessive targets and form-filling. As made clear in the Budget statement, public servants and trade unions have been co-operating closely with workforce reforms.

Public service restructuring – impact on jobs

The Budget announced a total cut of 40,500 Government jobs across the civil service and that all government departments will have to cut budgets by at least 5 per cent by 2008.

Back-office functions will be streamlined in the Department of Work and Pensions, leading to a headcount reduction 30,000 by 2008. The Inland Revenue and Customs and Excise will merge with 10,500 jobs to be cut by 2008. Administrative jobs will be cut in the Department for Education and Skills, with 31 per cent of its headquarters posts to go. The Government also plans to move 20,000 civil jobs out of London and the south-east to the regions.

The Budget predicts that £20 billion a year can be saved by cutting administrative budgets, reforming procurement, and achieving productivity gains from technology and workforce improvements. However, such reforms are unlikely to offer a quick payback and that they incur considerable costs up front.

It is vital that these proposals take account of the effect that relocation, redeployment and redundancies will inevitably make on the quality of service delivery, especially in the provision of face-to-face services. The civil service provides essential services, which must not be undermined by these reforms.

With regard to plans to move services out of the south-east, we welcome the commitment to regenerate the regions through new employment opportunities, but relocation of people must be done on a voluntary basis and there should be no compulsory redundancies.

In addition, dispersals must not result in the erosion of national bargaining arrangements. The TUC is committed to national bargaining in securing transparent and fair pay systems. Any moves away from national bargaining

would erode the principle of equal pay for work of equal value and would lead to increased administration costs as separate units develop their own pay and conditions systems.

Looking in more detail at the implications for the Department for Work and Pensions, the Chancellor announced overall cuts of 30,000 or 23 per cent of the workforce, with a further 10,000 redeployed. At the same time, the Government will expect to “*move resources to the front line to expand our successful service of personal advisers.*”

It is true that the development of personal advisers is one the Government’s success stories, and the TUC welcomes the expansion of their numbers. But there are other important jobs in the benefit system. Although information technology can make claims processing and paying benefits simpler and faster there are many jobs that still require human input. There is a real risk that the numbers of errors and delays in payment of benefits will increase, especially during the transition period.

The TUC is concerned that a cut in staff numbers on this scale threatens a collapse of morale among remaining staff and, counter to the key objective, could have a serious impact on the front line services to be delivered. Although the Chancellor emphasised his aim of freeing up resources to improve front-line services, the Department has already announced an immediate freeze in recruitment to its two bottom grades and strict limitations at Executive Officer level – the very people who do most of the Department’s work with its clients and the public.

Fairness for Pensioners

This was not a Budget that had much to say about pensions. The main measure was a one-off extra £100 to all pensioners over 70 on top of the winter-fuel payments to help cope with recent council tax rises. Any increase is welcome, although an across the board increase for all pensioners regardless of income is not entirely in line with the Government’s strategy of concentrating help on the poorest. But the big omission was women and pensions, where some highly progressive reforms suggested by the TUC and others could have been introduced to help low paid women workers at very modest cost to the Exchequer.

Moreover, the one-off across the board payment is not consistent with the Government’s argument against re-indexing pensions to earnings, namely that all

pensioners get the same. Had the current basic state pension increased in line with average earnings, at 4.4 per cent, it would have increased by around £3.40 in April 2004 rather than the £2.15 announced in the Budget report. The Chancellor could have re-indexed the pension for those over 70 at less cost than the one-off payment announced in the Budget. The TUC believes that only by restoring the link between earnings and pensions the Government can ensure that pensioners share in the nation's rising prosperity.

A small number of welcome measures were announced to encourage future pensioners to build up income for retirement. These included a number of the proposals called for by the TUC, including the introduction of a Pension Protection Fund.

Industry

As noted above, the Budget was noticeable for the absence of substantial measures to support manufacturing, other than the restatement of the extension of the scope of the R&D tax credit and some measures to improve venture capital support for small business and new business regeneration in local areas.

The Chancellor also sought to close the loophole he created in Budget 2002 when a 0 per cent corporation tax rate was established. As a result, many individuals had a strong incentive to declare themselves incorporated and take income in the form of dividends. This helps account for the spectacular surge in self-employment since April 2002, much of it bogus. Rather than abolish the rate, the Chancellor has increased the tax rate on small firm dividends to remove the incentive.

The TUC and film industry unions welcome the budget announcement that the current Section 48 relief will be replaced in July 2005 by a new relief that will typically cover 20 per cent of the production cost of British films (compared with the 15 per cent typically covered by the current Section 48 relief). This is on average an increase of 33 per cent per production. It is right to ensure that this relief is targeted at productions that have a strong British component, and we support tightening the definition of British Qualifying Status.

Science

The TUC welcomes the announcement (yesterday) that a ten-year investment framework for science and innovation will be published alongside the 2004 Spending Review. Within the priorities identified by the Government, we particularly welcome recognition of the need to invest in science and technology skills in education to ensure that future generations are equipped with the right skills. The TUC and unions will wish to contribute to the development of the Government's strategy for science and the ten-year investment framework.

Skills

The Budget contained a number of measures building on the approach set out in the Government's *Skills Strategy White Paper* published last summer, which aims to tackle the UK's longstanding skills deficit. The main two announcements in the Budget around skills policy were:

- a more detailed description of the *New Deal for Skills*, which was initially announced in last year's Pre-Budget Report
- a group of initiatives aimed at ensuring that all young people reach the age of 19 ready for higher education or skilled employment

In addition, the Chancellor announced the locations of the third tranche of Employer Training pilots and the Budget Report included further developments around the regional skills agenda and the role of migration in tackling skills shortages.

The *New Deal for Skills* will quite rightly make Jobcentres give greater priority to helping unemployed and economically inactive people acquire the skills necessary for them to achieve sustainable employment. In spite of the success of the New Deal programmes aimed at these two groups, there is widespread evidence that many jobless individuals continue to be caught in a "low pay – no pay" cycle because they are unable to acquire the necessary qualifications to achieve sustainable employment or to progress into better quality jobs.

In addition, the *New Deal for Skills* will also give employed people a single point of contact so that they can access appropriate provision to acquire existing learning entitlements (e.g. basic skills qualifications) and also forthcoming learning entitlements, such as the guarantee of an opportunity for every adult to gain a level

2 skills qualification. Trade unions will need to look at how the role of Union Learning Reps in the workplace can be utilised to assist employed and unemployed people using this particular New Deal programme to access work-based learning.

The launch of a *New Deal for Skills* and the extension of the Employer Training Pilots also brings us much closer to a national delivery system to underpin the forthcoming “Level 2 learning entitlement” which is at the heart of the Government’s Skills Strategy. However, over the longer term the Government will need to look at ensuring eligible employees can take advantage of this guarantee by having some form of right to paid time off to train in their workplace.

The Chancellor also announced the location of the third tranche of Employer Training Pilots that will commence in September of this year. Five of the new pilots will be located in the following local Learning and Skills Council areas: Lancashire, the Black Country, West Yorkshire, Cambridgeshire and Devon & Cornwall. There is also going to be a region-wide pilot in the North East. From this autumn these pilots will cover more than a third of England and the TUC is actively campaigning for a national programme along these lines to be launched as soon as possible after the pilots end in Autumn 2005.

The New Deal for Skills will also entail Jobcentres working much more closely with local Information, Advice and Guidance (IAG) partnerships so that “individuals have the advice and support they need to make decisions about training based on a full understanding of how it is likely to enhance their employability”. The Government is also intending to look at the idea of developing the concept of a “skills passport” that would hold a record of all training and skills that individuals have acquired. This would build on initiatives that are already well developed in the ICT and construction sectors.

The offer of training or education for all young people up to the age of 18 set out in the Budget is a welcome development. However the right to support being conditional on a responsibility to engage in learning must take account of personal circumstances.

There is much to welcome in terms of financial support for young people. In particular, the commitment in the short-term to extend the support available for young people in full-time education to unwaged trainees is a critical step in

ensuring a level playing field for young people choosing a work-based route. The extension of support to over 19s until they finish their course is also a welcome step forward.

The TUC will be responding to the consultation paper 'Supporting Young People to Achieve: Towards a New Deal for Skills', concerning the longer-term financial support arrangements for 16-19 year olds in the longer term.

Guidance will be reviewed on JSA severe hardship and estrangement regulations. This will help ensure that young people most in need receive the assistance they require.

The commitment to work towards achieving a minimum pay levels for apprentices will help ensure that there is at least a minimum platform that will protect young people and encourage them into apprenticeships. The expansion of Modern Apprenticeship programmes is welcome along with measures to increase both the quality and quantity of training.

Reforms to advice, guidance and support structures for young people to better fit need are also welcome. However it is important to ensure that appropriate resources and training are provided to this end. These reforms will also include ensuring parents have access to relevant advice and information, which is critical given the central role that parents often play in helping their children in career choices.

Child poverty – the Child Tax Credit

Last December the Pre-Budget Report announced that, from April there will be a very welcome increase in the Child Tax Credit, of £3.50 a week – about £3 over the increase that would have been required to uprate CTC in line with average earnings. The Government estimate that this is what is needed to meet the interim child poverty target of reducing the number of children living in poverty by a quarter by 2004.

As a result of this increase families with children will be £175 a year better off in real terms, and those in the poorest fifth of the population will be £425 a year better off. This is very welcome – hundreds of thousands of the most vulnerable

children will benefit, and the willingness to commit this level of resources indicates that the Government is serious about child poverty.

This must also be seen alongside the Chancellor's promise to create 1700 children's centres around the country, with increased spending on early years education and childcare to increase by £669 million by 2008. This is a significant step towards the childcare support unions have long demanded.

Working Tax Credit

The Chancellor announced that the Government will be consulting on phasing out payment via employers of Working Tax Credit. At present the Child Tax Credit is normally paid direct to claimants, but the Working Tax Credit, like the Working Families Tax Credit before it, is normally paid through the pay packet. In the Red Book, the Treasury argues that, now that tax credits are well-established, the original reasons for administering them in this way – reducing stigma, reinforcing the idea that tax credits are a reward for work – are no longer as important, and that reducing the regulatory burdens on business is a higher priority.

There are also reasons why unions will welcome this move. Receiving tax credits via their employers puts workers in a doubly dependent position: relying on employers for their wages *and* their benefits. Phasing out payment via employers will increase the independence of low paid workers.

This reform will also reduce the likelihood that WTC will have the effect of subsidising low pay. Unions have always had some concerns that less scrupulous employers might use tax credits to hold down pay. Evidence indicating that this has happened is scarce, which has encouraged us in our general support for the tax credits, but common sense suggests that at least some employers who are paying the tax credits in their employees' pay packets will be tempted by the opportunities for holding back pay rises. This will be less likely to happen when the employer no longer administers WTC. The TUC intends to respond to the Government's consultation on the implementation of this reform.

Although most of the news about tax credits has been very positive, one item has not been. The tax credit income thresholds – the points at which tax credits start to be withdrawn as income rises – have been frozen. As a result, workers who receive a pay rise in line with inflation will see their net incomes increase by less than

inflation. This failure to uprate will not help to ‘make work pay’ and is therefore at odds with the rest of the Government’s welfare-to-work strategy. Moreover, the maximum eligible costs for the childcare element of Working Tax Credit have been frozen at £135 per week for one child and £200 for two.

Other welfare reforms

Among the other welfare reforms announced by the Chancellor were a series of measures designed to increase the number of people moving off benefits and into employment.

- **New Deal for Partners (NDP)** – will be enhanced and opened up to anyone not in full-time employment in a family that receives the Working Tax Credit.
- **The worksearch premium** – in these families, people who join the NDP will be eligible for an extra £20 per week.
- **The job preparation premium** – similarly, the Government will pilot a £20 premium, lasting up to 26 weeks, for anyone on an incapacity benefit willing to “undertake a relevant activity that supports a return to work.”
- **Fair Cities** – in three cities, initiatives will be launched to help people from minority ethnic groups to get jobs.
- **Helping poor people to keep their savings** – from April 2006, the threshold at which a claimant’s savings begin to reduce the amount they can receive in means-tested benefits will be doubled to £6,000.

The new premiums for people looking for work are similar to the Labour Market Benefit, first demanded by the TUC more than ten years ago – we believe that they will help to keep economically inactive people in touch with the world of work, and thus increase the likelihood that they eventually get new jobs. The TUC has been increasingly concerned that the New Deal programmes are least effective in those cities with large black and minority ethnic populations, so we are very glad to welcome the Fair Cities initiative. And we have been increasingly concerned that the capital rules in means-tested benefits discourage saving, so the planned increases are also very positive.

National Minimum Wage

As set out in the Budget Red Book, the Government has announced that the National Minimum Wage will increase from 1 October 2004. The new rates will be £4.85 for adults and £4.10 for workers aged 18-21. In addition, 16 and 17 year

olds will be protected for the first time. The minimum wage for this age group will commence at £3.00 per hour.

These measures are very welcome. The real value of the minimum wage will rise, as the 7.8 per cent increase to the established rates is more than twice the predicted growth in inflation and average earnings. The establishment of a young workers rate for 16/17 year olds is a victory for trade union campaigning. Some 16/17 year olds are badly exploited at the moment, with pay rates as low £1.25 per hour. The TUC calculates that 7.5 per cent of younger workers will get a pay rise, which will benefit some 50,000 16 and 17 year olds.

